



Memorandum

TO: HONORABLE MAYOR AND
CITY COUNCILMEMBERS

SUBJECT: HOUSING IMPACT FEE
NEXUS STUDY

FROM: Councilmember Johnny Khamis
Councilmember Pete Constant

DATE: June 1, 2013

APPROVED:

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RECOMMENDATION

Reject the staff recommendation to “direct the Housing Department to conduct a nexus study analyzing the impact that residential development has on the need for affordable housing in San José and to return to the City Council with recommendations.”

OUTCOME

Savings of up to \$75,000 in costs to Fund 448 – Multi-Source Housing Fund and in the considerable staff time that would be consumed in processing an RFQ, managing a consulting contract, analyzing data, and preparing recommendations for the City Council.

BACKGROUND

There is no question that it is important to the continued growth and success of San José that we have a wide diversity of housing options available throughout the City that meet the needs of all types of workers – from highly educated Ph.D.-level scientists and mathematicians, police officers, firefighters, teachers, service workers, small business owners, and even high-level executives. These diverse housing options must include rental and for-sale units, high-density units, single-family homes, and efficiencies. Among these options, affordability is an important consideration. Imposing a fee on developers who are building housing, however, will achieve exactly the opposite outcome. Instead of making housing affordable, it will either further restrict the housing supply or raise the cost of new for-sale and rental housing. To believe that increasing the cost of housing will create more affordability turns logic on its head and requires the willful rejection of the most basic of economic theories – that of supply and demand.

ANALYSIS

According to economist Christopher Thornberg of Beacon Economics (www.beaconecon.com), recent data shows that throughout Santa Clara County home prices are experiencing a steep upswing driven by low inventories. As of April 2013, the monthly housing inventory supply is at 1.8 months, the lowest among Bay Area counties. The ratio of home costs to rental costs has

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fallen below the 1:1 equilibrium, with rental costs increasing at an even faster clip than the price growth of for-sale units. Mr. Thornberg also points out that housing starts are being outpaced by the growth in demand. Therefore, the only sensible, real-world solution to the rising cost of housing is to increase the supply of housing.

Here in San Jose, recent data shows that:

- The average single-family home is listed at \$729,642, with a median asking price of \$655,000. (Source: <http://www.trulia.com>)
- The average price for a condominium or townhouse is \$415,338, with a median asking price of \$386,500. (Source: <http://www.trulia.com>)
- The average monthly rental rate is \$1,837. (Source: <http://www.citiesassociation.com>)

How would a Housing Impact Fee affect the supply of housing and housing affordability?

- A Housing Impact Fee would achieve exactly the opposite outcome desired by the City Council and the Housing Department – it will result in the construction of fewer housing units and will make those fewer units less affordable. Applying the Mountain View housing impact fee rate of \$10 per square foot, the cost to build a 1200-square-foot condominium would increase by \$12,000. For a 1500-square-foot condominium, costs would rise by \$15,000. In a medium-sized development of 200 units, the cost-increase could average anywhere from \$1 million to \$3.2 million, depending upon the size mix of the units.
- In the worst-case scenario for renters and purchasers, the fee would be passed on to them completely, driving rents and home prices higher. For the builders of rental properties and the purchasers of for-sale units, it will not only drive up the initial cost of housing, but on-going costs that are linked to property values, such as insurance costs and property taxes.
- In the best-case scenario for renters and purchasers, 100% of the fee would be fully absorbed by project investors. Unfortunately, this would leave these creators of our housing supply with fewer dollars to spend on other housing projects in our community. Reducing the capital available to build housing would result in less housing, not more.
- It runs completely counter to the City Council's efforts to cut impact fees in order to incentivize high-density, transit-oriented projects in North San José and high-rise development in the Downtown core. The fee will also hinder the city's efforts to attract investors to build out the Urban Villages prescribed in the City's Envision 2040 plan.

Beyond the detrimental effects to housing costs and/or supply, we would note that numerous bills are under consideration by the California Legislature that would directly or indirectly expand funding for government-directed affordable housing projects including:

- AB 532 (Gordon)
- AB 952 (Atkins)
- SB 470 (Wright)
- SB 409 (Emmerson)
- SB 391 (DeSaulnier)

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With so many pieces of legislation affecting affordable housing resources available to the City of San José in the pipeline, it is unnecessary for the City to begin to look at imposing new costs on housing developers.

CONCLUSION

Rejection of the staff recommendation to pursue a Nexus Study for a potential Housing Impact Fee will save the City \$75,000 and numerous hours of staff time and will move us away from imposing additional costs on the very projects we need to move forward in order to more closely match the demand for housing with lagging supply and increase the overall affordability of housing options within San José.